

1 UNITED STATES DISTRICT COURT
2 WESTERN DISTRICT OF WASHINGTON

3 CELL THERAPEUTICS,)
4)
5 Plaintiff,) No. C 07-310
6)
7 v.) Seattle, Washington
8)
9 THE LASH GROUP,)
10)
11 Defendant.)
12)

13
14 BEFORE THE HONORABLE JAMES L. ROBERT, DISTRICT JUDGE

15 REPORTER'S TRANSCRIPT OF PROCEEDINGS

16 MAY 23, 2008

17 APPEARANCES:

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21 TOM SUDDATH
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1 SEATTLE, WASHINGTON FRIDAY, MAY 23, 2008

2 HON. JAMES L. ROBERT, DISTRICT JUDGE 9:04 A.M.

3 PROCEEDINGS:

4 THE CLERK: Case C 07-310, Cell Therapeutics versus
5 The Lash Group.

6 Counsel, please make your appearance.

7 MR. DUNNE: Your Honor, for the plaintiff I'm Dan
8 Dunne from Heller Ehrman. And I'm here with my partner Brendan
9 Mangan and Don Wyatt, who is counsel in-house for Cell
10 Therapeutics.

11 MISS THORNTON: Good morning, Your Honor. I'm Laurie
12 Thornton from Corr Cronin Michelson Baumgardner and Preece
13 representing The Lash Group.

14 Joining me at counsel table is Tom Suddath of
15 ReedSmith and Elizabeth Fenton, also for defendants. They have
16 both been admitted pro hac vice.

17 And Mr. Suddath will be handling the argument.

18 THE COURT: Counsel, we're here for argument on what
19 is in the docket as docket number 26, Lash's motion for
20 judgment on the pleadings; and I'm going to give you 20 or 25
21 minutes or so per side to argue this. I may well interrupt you
22 as we go along to ask some questions.

23 Let me tell you a little bit about how I view this
24 case so that you can shape part of your argument. We are here
25 on the motion to dismiss, and to me the wellspring of all law

1 in the Ninth Circuit on this issue is -- comes out of the
2 Mortgages case. I'm somewhat amazed at the brevity of
3 Mortgages, but that was the decision that we have to work with.
4 There is substantial additional authority that has flowed forth
5 from Mortgages, which seems to me to be dispositive of certain
6 of the arguments that have been made, some by both sides in
7 this matter.

8 I note that there is a declarative, flat,
9 black-letter statement in Mortgages at one point that says
10 where one or more persons have committed a fraud upon the
11 government in violation of the F C A, each is jointly and
12 severally liable for treble damages and statutory penalty, and
13 that is indeed the case. They then go on to discuss the
14 question of indemnification or contribution.

15 It seems to me that the question that I'm being asked
16 is is there a ban on indemnification or contribution, and I
17 think that's a question that you all need to address with some
18 care here. And you might want to spend some time taking the
19 claims which are found in the complaint and either convincing
20 me that those arise out of the underlying conduct or they are
21 independent.

22 I will tell you, largely because of my own
23 background, I have some familiarity with the P S L R A, which
24 has analogous, not identical but analogous, ban on
25 indemnification and contribution claims against a settling

1 party, and I'm aware of the two lines of authority that arose
2 out of that and how we look at those claims in order to
3 determine if they are covered or not.

4 It seems to me that under different terms there has
5 been the importation or maybe exportation of some of those same
6 standards into this area.

7 So that's what I have been looking at in terms of
8 trying to understand this case, and I'll hear from Lash first;
9 and you may reserve some of your time.

10 MR. SUDDATH: Thank you, Your Honor.

11 Good morning, Your Honor. My name is -- as
12 Miss Thornton said, I'm Tom Suddath. I'm from ReedSmith, and
13 we represent The Lash Group in this case.

14 Your Honor, the -- in our papers we have -- our
15 motion for judgment on the pleadings is based upon the fact
16 that each of the claims in the complaint, as pled, would have
17 the effect of giving C T I indemnification under the False
18 Claims Act, and under the Mortgages case and its -- the cases
19 that follow it from other jurisdictions any claim which has the
20 effect of giving indemnification to another party for liability
21 on the False Claims Act is a claim for indemnification and
22 therefore cannot be allowed to proceed.

23 The -- as alleged in the complaint, Your Honor, C T I
24 is a drug company which --

25 THE COURT: Why don't you -- I think I understand.

1 MR. SUDDATH: Okay. Very good. Then I'll go right
2 into the argument, Your Honor.

3 The -- their claim is that it seeks to recover 10.5
4 million dollars which it paid to the government to settle False
5 Claims Act allegations against it, and it claims that the -- it
6 paid these damages because it relied upon advice provided to it
7 by documents. Under the Ninth Circuit decision in Mortgages,
8 all these claims must be dismissed because they have the effect
9 of -- if prevailed upon, to have Documedics repay through
10 indemnification the damages which it paid to the government.

11 THE COURT: Has anyone outside the Ninth Circuit
12 followed Mortgages? You mentioned a moment ago the other
13 courts that have followed Mortgages. Seems to me there are
14 other courts that have construed the statute. Has anyone
15 expressly adopted the Mortgages language?

16 MR. SUDDATH: Your Honor, they have. There have been
17 a number of the cases we cited in the -- in our papers. One
18 case comes to mind is the -- as it goes to the issue of
19 independent claim which the Court raised, is the Prabhu case
20 out of the District of Nevada. We also have the Miller case
21 out of the District of the District of Columbia, which
22 addressed the issue of recovery for alleged independent claims
23 under the False Claims Act, and both of them --

24 THE COURT: The Nevada case, they didn't have a
25 choice. You're telling me that there's a D.C. circuit

1 authority for this.

2 MR. SUDDATH: No. The District Court of the District
3 of Columbia.

4 THE COURT: Okay.

5 MR. SUDDATH: The cases which have addressed
6 Mortgages, we had the Madden case out of the Ninth Circuit
7 also, which again addressed the issue of whether or not the
8 claims under the False Claims Act -- if the nature of the claim
9 would have the effect of providing indemnification, and those
10 claims are not allowed to proceed under the False Claims Act.

11 THE COURT: Is there a better term than independent
12 claim to describe the test that you're proposing?

13 MR. SUDDATH: The -- I think that the issue would be
14 whether or not the ability to recover or the damages that are
15 sought are dependent -- are damages that are caused by or
16 dependent upon the defendant's -- in this case The Lash
17 Group's -- whether the damages that are allegedly caused by The
18 Lash Group's actions are inextricably tied to the damages that
19 the -- in this case C T I claims that it had paid.

20 And what I mean by that, Your Honor, is that in this
21 case the -- all the claims that C T I asserts are all dependent
22 upon the damages caused by the actions of The Lash Group. But
23 for the advice given by The Lash Group, according to the
24 allegations in the complaint, C T I would not have been
25 damaged.

1 What they argue is that, because we caused them to
2 violate the False Claims Act, they have been damaged. We in
3 effect, according to their allegations, participated in the
4 fraud, and as a result of their reliance upon our advice
5 they -- as pled, they were required to pay a 10.5
6 million-dollar -- 10.5 million dollars to the U.S. Attorney's
7 Office to settle these claims.

8 THE COURT: Let's assume for a moment that they -- in
9 an independent action, so let's set aside any of those
10 procedural questions that are discussed sometimes -- and they
11 say, because of this entire episode our reputation has been
12 damaged to the tune of 25 million dollars, we can demonstrate
13 to you that we have suffered, and we have an expert who will
14 prove that, whatever. Would you then say that that is an
15 indemnity or contribution claim?

16 MR. SUDDATH: I would say that it is not -- it is a
17 claim that is not independent of their claim for
18 indemnification under the False Claims Act because that claim
19 of loss of reputation, if you will, is -- is a claim that
20 arises out of the actions of The Lash Group which caused them
21 to face liability under the False Claims Act, and as a result
22 of that everything is tied together. You can't divorce the
23 loss of reputation, if you will, from the fact that they were
24 exposed to liability under the False Claims Act.

25 The cases which have addressed this that have allowed

1 the claims for independent counterclaims to go forward have
2 been the types of claims where there's been an allegation
3 against the qui tam relator that they have libeled or that
4 there had been malicious prosecution or that there had been a
5 misappropriation of trade secrets. Those claims, those damages
6 are independent of any liability that the -- in this case C T I
7 would have.

8 THE COURT: So what I hear you saying is you're
9 really suggesting to the Court, then, that you want to adopt
10 more of an interrelatedness test to characterize the degree of
11 overlap.

12 MR. SUDDATH: I think that the issue is, Your Honor,
13 that the -- whether the damages are -- whether the damages that
14 they are seeking are damages that flow from the -- their
15 potential liability under the False Claims Act, as opposed to
16 being independent of any liability that they may face under the
17 False Claims Act.

18 And I think that, you know, one case that addresses
19 this issue is the Prabhu case out of the District of Nevada
20 where -- that was a case that we cited in our papers -- where
21 the -- there was a claim, third-party claim, brought by a --
22 somebody who had been named as the defendant in a False Claims
23 Act case, and in that case they brought -- the defendant
24 brought a third party claim against a party which it alleged
25 had participated in the fraud by assisting the defendant in

1 bringing -- in submitting false claims.

2 And in that case the district court allowed certain
3 claims to go forward as they get -- certain counterclaims
4 against the relator, those counterclaims, if I'm correct, were
5 counterclaims for libel and perhaps malicious prosecution but,
6 to the extent they were seeking to assert claims against a
7 third party for their alleged participation in the underlying
8 conduct, the court said those are not independent claims
9 because the effect of that, of allowing those claims to go
10 forward, would be in effect to give the defendant or the qui
11 tam defendant the ability to receive indemnification under the
12 False Claims Act; so what I would say, Your Honor, sufficient
13 to look at the effect of the claim and not how well it's pled,
14 not how well it's dressed up, because you can -- as the courts
15 have pointed out, through clever pleading a number of parties
16 have tried to escape the rule under Mortgages.

17 The other case, Your Honor, I would point out --

18 THE COURT: Let me stop you before you move on.

19 MR. SUDDATH: Certainly.

20 THE COURT: It seems to me if you read Judge
21 George's -- Chief Judge George's ruling he starts with a
22 flat-out statement the qui tam defendants' claims include,
23 inter alia, breach of contract, breach of the covenant of good
24 faith and fair dealing, breach of fiduciary duty, fraud,
25 negligent misrepresentation. Sounds familiar from somewhere.

1 Then he goes to say, in what really seems to be the linchpin to
2 this holding, each of the third party claims seeks to hold the
3 third party defendants liable to the extent that any false
4 claims are proven at trial.

5 And that seems to be the key to him to unlocking
6 this, and the question that I would ask C T I, if we follow
7 that line, is how is it that any of your claims found in the
8 complaint are not based on false claims that are proven at
9 trial? And I want to make sure I understand that that's the
10 position that you're endorsing.

11 MR. SUDDATH: Yes, Your Honor. The position that we
12 are taking is that the -- that our liability in this case
13 arises out of our actions in -- our potential complicity, if
14 you will, in submitting the alleged false claims, and that the
15 damages that the defense -- that C T I is seeking to recover
16 from us are damages that are -- that -- all damages flow from
17 the -- their potential liability under the False Claims Act.

18 It's all tied together. You can't -- it's not a
19 situation such as arises in some of these cases where it is an
20 independent claim for libel; it's an independent claim for
21 misappropriation of trade secrets. For example, if a qui tam
22 relator were to have, during the course of their employment,
23 taken certain papers or had destroyed certain property, then in
24 that case, you know, the liability of the qui tam relator for
25 that claim is not in any way tied to any liability under the

1 False Claims Act. It's completely separate.

2 THE COURT: Let me stop you. Pardon me for taking a
3 hatchet to your facts here, but I'm going to call C T I
4 basically a drug company and I'm going to refer to Lash
5 basically as a marketing expert. Let's assume that there is a
6 distinction between Lash's efforts, some of which may be
7 covered by the False Claims Act, and Lash's efforts which were
8 negligent or just downright not very well done.

9 Are you telling me that they -- those kinds of
10 claims, the latter category, would also be barred?

11 MR. SUDDATH: Yes, Your Honor, I am.

12 THE COURT: Why?

13 MR. SUDDATH: Because everything -- all those -- all
14 those claims, Your Honor, arise out of the same set of facts,
15 and the damages that they're seeking -- again you have to look
16 at -- you have to look at the -- the effect of allowing those
17 claims to go forward. And if the effect of allowing those
18 claims to go forward is to allow C T I, the drug company, to
19 receive indemnification for any -- for any of their actions as
20 to which we may have participated as part of those actions
21 but -- it would allow them to receive indemnification under the
22 False Claims Act for -- if you will, under your scenario, for
23 actions that are -- they all arise out of the -- the same core
24 set of facts, which is the advice that we provided to C T I was
25 wrong, the advice that we provided to C T I caused them to

1 violate the False Claims Act. Everything is tied together.

2 In your scenario you just can't divide, you can't
3 divorce the damages. All the damages flow from the same set of
4 facts.

5 THE COURT: Well, it seems to me that there -- I've
6 not worked my way through this. This is a judgment on the
7 pleadings motion.

8 MR. SUDDATH: Correct.

9 THE COURT: If I have to get in and start examining
10 the facts and making factual determinations, then don't I get
11 flipped into a Rule 56 motion and then aren't they entitled to
12 the presumption that we're into the facts, that it would be
13 better to have a jury determine this?

14 MR. SUDDATH: Oh, I -- well, I don't think you -- I
15 think the Court can make its determination based upon the
16 pleadings that are in the case at this point.

17 THE COURT: Well, what do I do when I get to some of
18 their claims where you think their claim means one thing and
19 they think it means something else? I mean doesn't that
20 require me to engage in a factual analysis?

21 MR. SUDDATH: Such as what, Your Honor?

22 THE COURT: At various points, you know, for breach
23 of terms of service in the service agreement. That requires me
24 to then engage in an analysis of what was the scope of services
25 under the service agreement in order to draw this line of

1 violation.

2 I heard you use a phrase I haven't heard in a long
3 time, the operative core of central facts or whatever the old
4 standard used to be. Are you saying that where you are is that
5 we've got this one set of activities, some of which may be --
6 contribute to false claims, some of which may not, but they are
7 so intertwined that the policy is I ought to reject any effort
8 to try and segregate those and find them all related to the
9 false claims?

10 MR. SUDDATH: What I'm saying, Your Honor, is that if
11 you -- if the Court looks at the pleadings, looks at the
12 complaint, the Court can make a determination based upon the
13 record as it stands and that the record as it stands would -- I
14 think there is a basis for the Court to conclude that all the
15 damages as pled in the complaint are damages that arise out of
16 their -- arise out of the faulty advice that we allegedly gave,
17 which caused them to face liability under the False Claims Act,
18 whether those damages are damages for -- the direct damages or
19 business damages, because, but for our negligent advice,
20 according to Lash, but for that, they wouldn't have faced any
21 damages, and the advice is advice that -- again it goes back to
22 the advice that we provided, which allegedly caused them to
23 face exposure under the False Claims Act.

24 THE COURT: I understand your argument. Why don't
25 you go ahead and make any other points you want to make and

1 then we'll save you some time for rebuttal.

2 MR. SUDDATH: Thank you, Your Honor.

3 I would -- Your Honor, I would just point out that
4 the -- in this case C T I has not cited any case allowing for
5 indemnification under the False Claims Act, that every court
6 that has addressed this issue has agreed there's no right to
7 indemnification under the False Claims Act, and the key again
8 is what is the effect of allowing that claim to go forward. If
9 the -- if C T I were to prevail and if the effect of that is to
10 effectively provide for indemnification, then that claim is
11 barred under the False Claims Act.

12 And that stands also, Your Honor, no matter whether
13 it's a claim for negligence or there's a claim for breach of
14 express or implied warranty or express or implied contribution.
15 As we said in our papers, you know, the claim is whether it's
16 an express claim for indemnification, contractual claim for
17 indemnification, or implied claim for indemnification. If the
18 effect is to allow for indemnification, then that claim is
19 barred.

20 The one case that -- the single case that they --
21 they cite which -- as enforcing a contractual indemnification
22 cause, if you will, in a False Claims Act case is the Watkins
23 case out of the District Court out of the District of Virginia,
24 and that was a case, Your Honor, where the courts didn't
25 address this issue. The issue before that court was simply

1 whether or not to affirm an arbitrator's award. And the court
2 decided it under contract principles. In fact in that case,
3 Your Honor, the parties had agreed that the issue of the
4 potential liability under the False Claims Act would not be
5 before the arbitrator, that the issue before the arbitrator was
6 simply interpretation of contract law.

7 So, as the -- in this case, Your Honor, there has
8 been -- we found no case that would support C T I's position.
9 C T I has provided no case which would allow them to proceed in
10 this case for -- if the effect of any of their claims, no
11 matter how they're pled -- if the effect of that would be to
12 provide indemnification to them.

13 Thank you, Your Honor.

14 THE COURT: Thank you, counsel.

15 Mr. Dunne, are you up? All right.

16 MR. DUNNE: Good morning, Your Honor.

17 Lash starts its argument with the Mortgages case, but
18 that case is simply an application of the False Claims Act, and
19 so you really need to start with a review of the language of
20 the False Claims Act. And the first question that you have to
21 ask there, is there any language in that act that bars claims
22 by one defendant against another for independent rights under
23 contract of tort? And clearly there's not, and our case that
24 we cited, Piqua, says that.

25 The next question, is there anything in the

1 legislative history that indicates that there is a
2 Congressional intent to do so? Again there's nothing in the
3 legislative history. The Mortgages case refers to the
4 legislative history of Congress's original intent of setting a
5 rogue to catch a rogue. Well, that would protect qui tam
6 plaintiffs from retaliation, but it has nothing to do with
7 claims by one defendant against another defendant, and I'll
8 explain that a little more in a minute.

9 So, understanding that there is absolutely no support
10 in the False Claims Act to bar the claims that we have brought
11 in this case, then you have to take a look at what other law
12 might apply and what policies might apply.

13 THE COURT: Well, isn't the linchpin to your argument
14 your use of the phrase independent right?

15 MR. DUNNE: No. It actually is not, because there's
16 no bar against contribution or indemnification. The court
17 referred to the P S L R A, and the P S L R A there is a statute
18 that bars indemnification contribution claims against a
19 settling defendant. We were the settling defendant. Policy
20 there is to promote settlement. It's clearly expressed.

21 And so that would be a very different application.
22 There you see a policy. There is no policy that's stated in
23 the False Claims Act to protect an innocent settling or to
24 prevent an innocent settling defendant from recovering against
25 another defendant.

1 THE COURT: What do you do with the language in
2 Mortgages where -- it's a per curiam opinion. For the reasons
3 set out below we conclude there is no right of indemnity or
4 contribution among participants in the scheme to defraud the
5 government in the violation of the F C A.

6 MR. DUNNE: You go back and you look at what the
7 court decided in the previous page before it made that
8 decision, and it did just two things. It started by saying
9 Congress did not intend to create a claim or cause of action or
10 right of action for indemnification in the statutory scheme.
11 So it reviewed the statutory scheme and said, we don't find a
12 Congressional intent to create a right of one defendant against
13 another. That doesn't mean that your preexisting contractual
14 rights are valid.

15 The second thing it does -- and this is what Judge
16 Coughenour decided in the Capital One case -- is that they
17 applied the Court v. Arb factors to see whether under federal
18 common law a defendant could imply a claim for contribution or
19 indemnification as part of the statutory scheme, applying the
20 various factors that Court v. Arb applied; and the court found
21 that it didn't. That's all that's going on in Mortgages.

22 So it's looking at the implication, the existence or
23 implication of a right, not bar or prohibition against a
24 preexisting, separate right. So we have an independent,
25 contractual, indemnification right, and we have independent

1 claim for professional duties from a professional that they
2 comply with their due care.

3 And the Court has focused on independent, so I'd like
4 to address some other issues, but let me first focus on your
5 questions about what is independent.

6 Not all --

7 THE COURT: Excuse me. Before you get to that one,
8 can you give me any case in which a court has permitted a
9 contractual indemnification right? In this circumstance.

10 MR. DUNNE: Yeah. The case from the Eastern District
11 of Virginia.

12 THE COURT: The Eastern District of Virginia, I mean
13 I've read that case, and what it says is we're affirming the
14 arbitration ruling.

15 MR. DUNNE: Right. But you would overturn an
16 arbitrator if an arbitrator completely refused to follow the
17 law; and if Mr. Suddath's argument is accepted that it would be
18 a complete refusal to follow the law, would be to allow such a
19 claim to proceed.

20 THE COURT: I just heard him tell me that they didn't
21 even get to that question.

22 MR. DUNNE: We have a different reading of the case,
23 because the case decision is the district court affirmed that
24 there was not a refusal to follow the law by allowing
25 indemnification because the contract did not exclude F C A

1 claims. So I think there's not -- more importantly, there's no
2 case that has been cited by the defendant in which a court has
3 prohibited contractual indemnification claim, and I want to
4 talk about the difference between implied indemnification and
5 contractual indemnification, because I think that's central to
6 your question.

7 But let me before -- in case I may run out of time,
8 refer to the Court's decision in Madden, which says that there
9 are very serious due process concerns if a court willy-nilly
10 dismisses these kinds of claims just because they're against
11 various parties in a qui tam or False Claims Act case.

12 And here we've been adjudged of no wrongdoing; there
13 has been no finding of liability under the False Claims Act,
14 and I think there would be serious due process issues that
15 Madden recognizes, and Madden is subsequent to Mortgages.

16 If the court goes to page 4 of our brief, what we do
17 is we quote sections from the contract on which we rely, and
18 there are various duties that Documedics owed to us.
19 Documedics agreed in its contract that in performing its
20 services it shall meet generally-accepted performance standards
21 of similarly-situated, top tier, agent reimbursement companies;
22 so they agreed to a standard of performance. They agreed to a
23 standard that all their staff would receive all necessary
24 training and possess all the licenses and permits to fully,
25 properly, adequately perform all services.

1 They also stated that their job as the reimbursement
2 expert is to insure that providers are as well-informed as
3 possible as to all patient choices. They agreed to comply with
4 all applicable business conduct and regulatory guidance. Those
5 are duties they owed to us directly. We are not seeking to
6 imply from the False Claims Act and federal common law some
7 right that we don't have that isn't supported by either of
8 those applications.

9 Now, where is our right different from the implied
10 indemnification? Well, a contractual indemnification right
11 doesn't just depend on liability under the False Claims Act.
12 And you hit the nail on the head, Your Honor, when you quoted
13 the presumption in Mortgages that the third party claimant
14 violated the False Claims Act. So inherent in that decision is
15 a finding of a violation and a finding of wrongdoing.

16 Now, in their brief Lash calls us a wrongdoer over
17 and over and over. That would require serious factual
18 findings. That would require a trial. We have not been
19 adjudged to be a wrongdoer in any sense of that word; so they
20 recognize that they really have no basis in fact to argue or
21 advocate for a policy that we cannot recover because we're a
22 wrongdoer, because there has been no finding that we're a
23 wrongdoer.

24 But, going back to this independent claim, our
25 indemnification --

1 THE COURT: Counsel, is your position, then, that I
2 can draw no implication from the fact that you paid whatever it
3 was, 10.5 million dollars to settle a False Claims Act claim?

4 MR. DUNNE: Just as with a D and O insurance policy
5 in a securities case, the settlement of the case allows you to
6 draw no implication that the settling defendants engaged in
7 intentional wrongdoing which would vitiate their ability to
8 recover under the D and O policy. That also is an
9 indemnification contract, and the principles are relatively
10 similar there.

11 You could not under public policy be indemnified as a
12 securities defendant for intentional violations of the 33 act
13 or the 34 act. But, as we know, settling defendants are
14 reimbursed 99.9 percent of the time, and Your Honor certainly
15 assisted that effort in the Chubb v. Nordstrom case.

16 So it's like a D and O insurance policy where there
17 are allegations of intentional wrongdoing, but in the absence
18 of an adjudication that does not vitiate your right to
19 insurance indemnification. So that would be our position.

20 THE COURT: Well, but in the false claims context,
21 let's assume you have a contractual indemnity provision, you
22 have two parties named in the False Claims Act provision, and
23 there is a settlement by one of them. Your position, then,
24 would be that the presence of that contractual indemnity
25 provision would trump in effect the Mortgages holding that

1 there is not to be indemnity or contribution among defendants
2 in a False Claims Act.

3 MR. DUNNE: The settlement doesn't trump it. It
4 doesn't presume it either. You can't presume that there is a
5 violation. So in that action there must be proof of a
6 violation of the False Claims Act. So you've merely shifted
7 the location where that proof would occur; so if we were
8 adjudged to have willfully and knowingly violated the False
9 Claims Act, then Mortgages would apply, to the extent it
10 applies to dependent claims. It wouldn't apply to independent
11 claims but it would apply to dependent claims.

12 But there has to be that finding; otherwise there is
13 no due process; otherwise there's no basis on which to apply a
14 policy, because we're not a wrongdoer. So that's our point.
15 The settlement, as Your Honor knows, admits no liability. It
16 is a settlement of a risk, not of an act.

17 And our contention -- and this has to be accepted as
18 true for purposes of what we're doing here today -- is that the
19 basis upon which we had potential liability were the acts of
20 our agent sitting over here who sent letters to doctors or made
21 phone calls to doctors and said, you should be reimbursed for
22 all (unintelligible) uses who sent letters directly themselves
23 under their letterhead signed by him, telling Medicare carriers
24 you should reimburse for these off-label uses of Trisenox and
25 who themselves participated in appeals when Medicare carriers

1 had denied.

2 We're seeking contractual indemnification for their
3 acts, not for our acts, and we would be liable (unintelligible)
4 because they're our agent. So that's a significant difference.

5 Here's why the contractual indemnification claim is
6 independent. Documedics shall indemnify and hold C T I
7 harmless against all liabilities. Now, if our contract stopped
8 there our claim would be completely dependent and we would be
9 within Mortgages, because we would have to be found liable for
10 a False Claims Act violation to recover. That's what the
11 common law indemnification requires.

12 All these cases, these district court cases -- and
13 there aren't any other Court of Appeals cases, but all these
14 district court cases that dismiss indemnification claims are
15 dismissing common law indemnification claims, and that only
16 arises upon a finding of liability. That's different from our
17 contractual indemnification. We don't have to be liable under
18 the False Claims Act to recover what the rest of that says,
19 which is losses, costs, and expenses and damages arising out of
20 or resulting from willful misconduct or negligent acts of
21 Documedics. So that is an independent basis not dependent on a
22 finding of a False Claims Act violation. The language you
23 refer to in Mortgages presumed an also violation of the False
24 Claims Act, so we are outside of the case there.

25 They also are required to indemnify us for breaches

1 of any covenants or agreements or from any violations that they
2 make of federal laws, and it's our allegation -- if the Court
3 wanted to see the testimony on this to support it we've got
4 it -- that they have had people who worked on this contract
5 testify that they sent letters to Medicare that
6 misrepresented -- they sent the letters and they misrepresented
7 whether Medicare should reimburse for off-label uses of our
8 drug.

9 So again their violations, not our violations, give
10 rise to the right here. So to that extent we are outside of
11 Mortgages; we are independent. There's another way that we are
12 completely independent, and Mr. Suddath didn't address this,
13 but our -- we have a completely separate damage claim that has
14 nothing at all to do with the False Claims Act and the False
15 Claims Act settlement. It's disclosed in our initial -- our
16 supplement to our initial disclosures, and that's a motion
17 that's also pending before the Court, and it may help for us to
18 address that at the conclusion of this argument because I
19 think, now that discovery is closed, it's important to
20 understand what discovery was conducted on the damages.

21 But that damage claim would exist without any False
22 Claims Act proceedings whatsoever. If a case had never been
23 filed, if there had never been a qui tam case, if there had
24 never been a settlement, that damage claim would exist. And
25 here's what it is. It says that we learned in late 2004 that

1 Trisenox was not entitled to be reimbursed for off-label uses
2 and this was a large part of our sales, a large part of our
3 market.

4 There are competitive drugs that entered the market
5 in May of 2003, May of 2004. In two of our key off-label
6 indications, multiple myeloma and myelodysplastic syndrome. We
7 had built business plans on future sales through 2012 in those
8 areas, and all of a sudden at the end of 2004, despite the
9 incorrect advice we had received that those diseases were
10 properly reimbursed, we learned that they were not properly
11 reimbursed.

12 The company disposed of the drug, made a decision to
13 divest itself of that drug within months because the entire
14 business assumption was vitiated and eliminated. If we had
15 known that before, if we had never been misled into believing
16 that the drug was properly reimbursed, then in the normal
17 strategic planning the company would have made a decision to
18 divest early in 2004, and that would have occurred six months
19 earlier, and that would have saved 12 million dollars in
20 losses.

21 THE COURT: Which of your five causes of action do
22 those damages allegedly arise from?

23 MR. DUNNE: That arises both under the contractual
24 indemnification clause and from the negligent -- professional
25 negligence claim. So, in other words, they acted negligently

1 in the performance of services and therefore are responsible
2 for losses and damages under that section. And for
3 professional negligence in providing negligent advice to us on
4 which we reasonably relied in making corporate decisions, they
5 would be liable for those damages in that respect as well.

6 THE COURT: Is that your third cause of action,
7 counsel?

8 MR. DUNNE: I don't have the complaint in front of
9 me, but there --

10 THE COURT: First cause of action is declaratory
11 relief. Second cause of action is breach for service of the
12 terms of service in the service agreement. Third cause of
13 action is breach of the service agreement's contractual
14 indemnification clause.

15 So I mean I'm trying to find out which it is that
16 you're proceeding under.

17 MR. DUNNE: It is not the first. It is the second
18 and the third. And then there is a -- I don't know whether
19 it's the fourth or the fifth claim for professional negligence.

20 THE COURT: Well, let me read you what your damages
21 are alleged under that. It says, direct and proximate cause of
22 damage in the form of investigation, litigation, and settlement
23 expenses, including attorney's fees and costs.

24 I mean, doesn't sound to me like you've sought in
25 your complaint what you're now telling me you've got a cause of

1 action or damages for.

2 MR. DUNNE: Well, we've sought all other and further
3 relief that is just and reasonable, and we've filed in -- on
4 April 21st a supplement to our initial disclosures which lays
5 out this damage claim and provides the calculations for the
6 damage claim. Again that's subject to a motion to strike and
7 we could address that -- I don't know if you had intended that
8 we would today or not. I'd be prepared to do that.

9 So what is the test? The test, we would tell the
10 Court, is that a claim is dependent if the right of action
11 depends on a finding of a False Claims Act violation. Our
12 contractual claim does not depend on a finding of a False
13 Claims Act violation, nor does the professional negligence
14 claim. Certainly the (unintelligible) indemnification claim,
15 and this separate damage issue has absolutely nothing to do
16 with False Claims Act liability whatsoever. It has to do with
17 decisions made in the course of strategic planning and when
18 those decisions would have been made if information had been
19 conveyed differently, nothing at all to do with the False
20 Claims Act. So that under any of the tests that the courts
21 have looked at would clearly be independent.

22 THE COURT: Let me go back, though. It seems to
23 me -- isn't there a mutual indemnification clause?

24 MR. DUNNE: No. There are -- it's not a mutual
25 indemnification clause; it's a one-way indemnification clause

1 for the negligent acts of the consultant, services provided.

2 I might point out, Your Honor, this isn't in the
3 record because it happened recently, but Lash is a settling
4 defendant as well. Lash has settled the qui tam action. And
5 that case has now been dismissed, which is important because
6 one of the policies that you find in the courts, in the cases
7 that have been decided, that there be effective enforcement of
8 the False Claims Act and the government's ability to proceed
9 not be interfered with, so they will not allow counterclaims
10 and third party claims within the False Claims Act itself.
11 That's not an issue here, obviously. This won't involve --
12 another policy is to protect plaintiffs and whistle blowers
13 from retaliation.

14 THE COURT: I understand those arguments, counsel.
15 One moment, please.

16 Please proceed.

17 MR. DUNNE: We touched on very briefly, Your Honor,
18 the problem that Lash has now because the facts they have
19 argued are not the facts that are alleged in the complaint. I
20 would just point out that the allegations in the complaint are
21 that we did not violate the False Claims Act, which would
22 require us to have knowing conduct, and that has to be assumed.
23 To the extent that other facts need to be decided, as you said,
24 we would need a trial in order to do that.

25 So in the end this case boils down to a couple of

1 things. One is are there any policies that are actually
2 promoted by the rule that Lash Group asks for here, because we
3 haven't been adjudged to be a wrongdoer, we haven't been
4 adjudged to be liable, we are not suing a qui tam plaintiff,
5 and we are not interfering with the government's prosecution of
6 a False Claims Act. There are none of the policies that are
7 implicated here. There's no statutory language that support
8 it, so there really is no basis to extend the Mortgages case to
9 this case, because none of the policies line up.

10 What is -- as we have argued, is far, far more
11 apparent is not to take a sledgehammer to this and use it
12 against every False Claims Act defendant, but in cases where
13 there has been no finding of False Claims Act liability to use
14 the tools of the common law, which have been pled in the answer
15 here, include in pari delicto defense and unclean hands
16 defense -- and those are more refined -- to address whether or
17 not my client should recover based on the facts as they are
18 found.

19 THE COURT: Mr. Dunne, I used to despise when people
20 did this to me, and now it's my favorite thing to do. Turning
21 to Article 8, indemnification, is there a difference between
22 8.1 indemnification by Documedics and 8.2 indemnification by
23 C T I?

24 MR. DUNNE: I don't know, because 8.2 has not been
25 pled in this case, so no indemnification has been sought by The

1 Lash Group here.

2 THE COURT: It seems to me, if I take your argument
3 and apply it, what I'm going to do at that point is basically
4 create a situation where you're going to be suing them for
5 indemnification, they're going to be suing you for
6 indemnification, and it seems to me I'm back to in effect
7 violating exactly the policy that my betters have told me I'm
8 supposed to protect here.

9 MR. DUNNE: Which policy is that, Your Honor?

10 THE COURT: To not allow indemnification for either
11 violations of the False Claims Act or arguably settlements of
12 the False Claims Act.

13 MR. DUNNE: Well, I don't think you -- first of all,
14 we are not in that situation, so the only indemnification
15 claims are.

16 Secondly, until one is found to have violated the
17 False Claims Act you can't violate the policy by allowing
18 indemnification, so if we are innocent or merely negligent we
19 wouldn't have the standard to have been held culpable and
20 liable for violation of the False Claims Act. Remember, we
21 settled a risk, and there's nothing -- there's nothing unusual
22 here, because this is merely a contractual indemnification
23 claim.

24 And these happen all the time, and people settle
25 risks, and then they go and they litigate over the

1 indemnification rights of the settlement of that risk, and
2 typically it has to do with the negligence or willfulness or
3 gross negligence of another party, depending on the contract.
4 But there's nothing that we are asking for here that is any
5 different than a normal contractual indemnification case.

6 And the tools are there to prevent indemnification if
7 we have been found to violate the False Claims Act. And Lash
8 intends to put that case on as they have argued by making all
9 the factual allegations they did in their reply. But they need
10 to put that case on and they need to prove it. This is not an
11 appropriate decision to be made on a motion to dismiss.

12 THE COURT: I'm going to ask you this one more time,
13 and perhaps you can summarize your answer. What I hear you
14 telling me is that a claim for relief, based on damages in the
15 form of investigation, litigation, and settlement expenses,
16 including attorney's fees and costs, you think is not related
17 to the underlying False Claims Act and instead is a
18 free-standing contractual indemnity claim.

19 MR. DUNNE: The free-standing contractual indemnity
20 claim that we have is the one that is disclosed in our
21 supplement to the initial disclosures, which isn't fairly
22 described by that allegation, so it is not specifically
23 described with particularity in the complaint. I don't think
24 it needs to be under the law of the Ninth Circuit. That issue
25 in itself hasn't been addressed to the Court. It could be.

1 But the free-standing claim is a claim that in our
2 strategic decisionmaking the company would have divested itself
3 of the product six months earlier than it did and avoided 12
4 million dollars in losses.

5 THE COURT: Counsel, have I ever seen the
6 supplemental disclosure? Isn't that exchanged between the
7 parties?

8 MR. DUNNE: I believe it's filed with the Court.
9 Yeah. It's been -- it was filed -- if it hasn't been filed
10 with the Court, it was filed as an exhibit to Lash's motion to
11 strike the damages claim. And I don't know if Your Honor would
12 like to hear argument on that, because I think there are
13 some -- a couple of things that would be worth saying about
14 that.

15 THE COURT: Well, let's see if we get over this one
16 first.

17 MR. DUNNE: Okay. Thank you, Your Honor.

18 MR. SUDDATH: Your Honor, the -- couple of points I'd
19 like to respond to. This is -- this is not an ordinary
20 indemnification complaint. This is a indemnification claim
21 that arises under the False Claims Act. That under Mortgages
22 makes all the difference in this case.

23 And I think it's important, as the Court points out,
24 that you have to look at the complaint as alleged, not as
25 Mr. Dunne has argued, that what, you know, may have come out in

1 discovery, what they may hope to prove, what they may hope to
2 allege in a amended complaint, but in their complaint, as the
3 Court pointed out, their damages that they claim flow from the
4 causes of action as pled in the complaint are for the damages
5 arising out of the settlement of their complaint.

6 And I'll read from the complaint. It says, Lash
7 Group's advice and conduct caused C T I to incur the cost of
8 investigating, defending, and settling claims by the government
9 that reimbursement was mistakenly made for use of Trisenox
10 off-label. I don't think you could be any clearer that the
11 damages that they are seeking in this case are damages that
12 arise out of the fact that they were sued under the false
13 claims and they chose to settle that case.

14 Their due process argument, Your Honor, is -- I think
15 can be easily disposed of. The Madden case, that talks about
16 due process in the -- where there's a compulsory counterclaim
17 that a defendant may need to bring against a relator. If the
18 Court were to accept the due process argument in this case,
19 then effectively no court would be able to decide a motion to
20 dismiss.

21 They chose to settle this False Claims Act case.
22 They have received all the process to which they're due.

23 Mr. Dunne has made reference several times that
24 there's no finding of liability and therefore the court -- and
25 that makes a difference. That doesn't make a difference under

1 the cases as decided. Each -- many of the cases, Your Honor,
2 that we've cited have been cases that have arisen at either the
3 notion to dismiss stage or motion for judgment on the
4 pleadings.

5 One of the cases we cited was a heart doctor's case
6 which was a case directly on point where a defendant chose to
7 settle False Claims Act cases and then sought to bring an
8 indemnification claim against a third party. The court said,
9 under Mortgages you can't proceed.

10 The -- you know, C T I has also argued that there's
11 no case that has barred a contractual enforcement claim for
12 indemnification of the False Claims Act case. I would cite the
13 Court to the Hensel Phelps case in our papers, in which the
14 court made that conclusion, rejected a contractual
15 indemnification claim seeking indemnification under the False
16 Claims Act.

17 And then finally, Your Honor, I think it's -- you
18 know, if the Court -- again it's important to look at the case
19 as pled, not as they wish they had pled, not as they may seek
20 to plead, but I think it's important to look at what have they
21 pled in their complaint and what damages do they ask for. And
22 the damages -- and I'll refer the Court to their initial
23 disclosure, which is what they filed back when this case
24 began -- and it says C T I's damages relating to its claims
25 are: 10.5 million dollars paid to settle the qui tam suit with

1 the government; half a million dollars, close to, \$550,000 in
2 attorney's fees on the part of firms respectfully in defense
3 and settlement of the qui tam suit and related government
4 investigation.

5 The record as it stands now is just crystal clear
6 that the claims that they are seeking are claims and the
7 damages that they're seeking for those claims are damages that
8 arise out of the False Claims Act and arise out of the fact
9 that they chose to settle allegations against them made by the
10 U.S. Attorney's Office for their violation of the False Claims
11 Act.

12 We were not -- the government -- we were not a party
13 to that. They were the party to it. The government looked at
14 that, and they chose to bring the case against them. C T I
15 chose to settle those, and it's as a result of their settlement
16 of those false claims allegations that we're here before the
17 Court.

18 And again I would -- the last point I would make,
19 Your Honor, is the -- we again have to go back to the
20 complaint. We have to look at the complaint. We have to look
21 at the allegations in the complaint. They have dropped a
22 footnote saying, well, if the Court doesn't think there's
23 independent damages, then we can simply amend the complaint.
24 That in my view is an implicit recognition that as pled there
25 are serious problems with their complaint. They haven't moved

1 to amend the complaint. They're simply asking the Court --
2 they're saying that they may be able to do that.

3 In essence that's what they're attempting to do in
4 this supplemental disclosure. I'll address that if the Court
5 wishes at the conclusion of this, because I think that there's
6 very substantial issues related to that. But again what we
7 need to look at, Your Honor, is what is the current state of
8 the record of the pleadings that are before the Court. And the
9 court has to look at that and it has to decide under Mortgages
10 whether or not the effect of allowing those claims to go
11 forward if prevailed upon would have the effect of allowing
12 them to receive indemnification for liability under the False
13 Claims Act. That's what Mortgages stands for.

14 Thank you, Your Honor.

15 THE COURT: Thank you, counsel. The Court will take
16 this matter under submission.

17 Counsel, I'm going to say something that I usually
18 don't say. My policy is is that we're here to try cases and we
19 do a lot of that, and I do not suggest settlement conferences
20 because I think that we're here as the ultimate arbitrator of
21 disputes and some disputes simply need to be tried.

22 In this one it strikes me that the ship of
23 indemnification and the ship of independent claims passed in
24 the night. I don't know. If I recall correctly, didn't you
25 all go see Judge Theiler at one point?

1 MR. DUNNE: Yes, we did, Your Honor.

2 THE COURT: All right. You know, if you want to
3 renew those discussions, now you know a bit more about each
4 others' cases, I would urge you to do that with some dispatch,
5 because we're going to be issuing an opinion in this matter and
6 I suspect our opinion will simply give one side or the other a
7 feeling of greater confidence.

8 If you want to wait until that comes out and see and
9 then talk to the judge, that's certainly an option for you
10 also. It strikes me that you now know a bit more about your
11 case and that might be an appropriate time for you to take a
12 look at that subject again.

13 Other than that, the matter is submitted. Thank you,
14 counsel. Nice to see all of you here. It's nice to hear
15 well-done argument.

16 We'll be in recess.

17 MR. DUNNE: Thank you, Your Honor.

18 (At 10:03 a.m. proceedings were adjourned.)

19 --o0o--

20 I certify that the foregoing is a correct transcript
21 from the record of proceedings in the above-entitled matter.

22 \s\ Laurene Kelly
23

This 17th day of JUNE, 2008.